



(Clear Lake Independent Telephone Company Business Office)

Written testimony submitted March 13, 2001 by Janet Lovell and Thomas Lovell to the Senate Finance Committee, Subcommittee on Taxation and IRS Oversight for the "Preserving and Protecting Family Business Legacies" hearing on March 15, 2001.

Thank you for the opportunity to speak today.

My name is Jan Lovell. I'm an owner, assistant manager and vice president of the Clear Lake Independent Telephone Company, a local exchange carrier for Clear Lake and nearby Ventura, Iowa with a combined population of about 9,000 people in the heart of the Midwest. I'm here to speak to you today about the devastating impact the current federal estate tax can have on small businesses, which are the nation's most bountiful provider of new jobs.

Just two years after Alexander Graham Bell patented the telephone in 1876, my maternal great-grandfather Charles Woodford and some other community-minded entrepreneurs saw how important this invention would be to the new settlement of Clear Lake, Iowa. They saw how it could help the young businessman who was just hanging out his shingle on Main Street and how it could provide important connections for the townspeople, including many immigrants who left their loved ones behind to begin new lives in the fertile lands of the prairie.

Clear Lake Independent Telephone Co.
Clear Lake, Iowa

INCORPORATED:
1895

ACCESS LINES SERVED:
(Clear Lake and Ventura)
8,200

EMPLOYEES:
26

OWNERSHIP:
Family enterprise
(Fourth generation)

MAJOR COMMUNITY ACTIVITIES;
Public Library Building Campaign; United Way; Economic Development; Environmental Leadership (Recycling, Earth Day, Lake Water Quality); Community Event Sponsorship (Fourth of July, Christmas by the Lake, Arts Council); Clear Lake and Ventura Public Schools Capital Campaigns

The first phones were connected in 1878 and the company was incorporated in 1895. The company's original nineteenth century mission was to provide dial tone and a connection to the outside world. But as but as customers have desired new services and as technology has advanced, our twenty-first century mission has grown into offering a multitude of advanced telecommunications services ranging from wireless to high speed Internet to video conferencing. The importance of telecommunications has grown beyond any nineteenth century entrepreneurs' dreams. Today, it fuels economic development, it is a basic necessity for any industry and it is a lifeline for a rural community.

But this lifeline is in danger of being cut because of the federal estate tax.

Our company is just one example of a small, capital-intensive business that spends a lot of time, money and resources trying to plan how to pay the federal tax bill when a family member dies. My mother, two sisters and I are the majority owners of the company and my father and husband own stock in it as well. Instead of focusing our limited resources on meeting important telecommunications needs, we find ourselves spending time with insurance representatives and lawyers to help us find a way through the maze of complex estate planning rules and regulations to do everything we can to keep the company in business when an owner dies.

The next speaker will give you details on what happened to us the last time a major stockholder, my grandmother Esther Woodford Ashland, died. It's a story of how, in spite of all of our family's planning through the years, we still don't know if this company will survive the next estate tax bill when my parents pass on.

There are those who might ask "...what does it matter if this little telephone company in northern Iowa has to close its doors because of federal estate taxes?" To that question, I would submit to you that it does matter because even a small company like ours - with less than 30 employees - can have a strong, positive impact on a community's economy, an effect which ripples far beyond just the jobs for which we are responsible.

Our twenty-first century mission in this capital-intensive small business requires millions of dollars to deploy new broadband technologies and careful, strategic planning to determine which costly technology to deploy and when for our customers. Our earnings must be plowed back into the company network. We recently borrowed \$9 million to rebuild our urban infrastructure and lay the groundwork for futuristic broadband services. This is the largest single capital project we've ever done in the company and a historic debt load for the company. We are willing to take on this risk because we feel that our customers must have access to the same quality of communications as someone living in a large city.

This kind of planning and risk taking, combined with local ownership, has some very clear benefits for our community in terms of new jobs, service to the customer and having some control over our community's future. In a state with a dwindling population, Clear Lake experiences moderate but steady growth.

One example of this occurred last year when a North Iowa high-tech software supplier and service provider needed to expand. Because of our local ownership and management and the advanced infrastructure we had in place, we were able to respond immediately to their intensive data needs. So instead of Kingland Systems Corporation

moving to another part of the country, we were able to help them re-locate here and expand in Clear Lake, providing 85 computer engineering and software developer jobs.

In contrast, we are surrounded by larger communities which are served by regional operating companies and others which are the result of mega-mergers. They haven't deployed high speed Internet access like DSL such as we have done. There is a waiting list to have basic phone service installed. There is no actual person to talk with face-to-face to answer questions. Offices have been closed and jobs lost in the name of corporate efficiency. Our rural areas are particularly hard hit because distant corporate managers can't cost-justify deploying advanced services to sparsely populated areas. And so the rural areas become disadvantaged simply because of where people live.

In Clear Lake, we install telephones within 24 hours or the same day whenever possible. The old-fashioned creed of "the customer is always right" is followed with the same zeal as when my grandfather was managing the company. Our customers are our neighbors. When we see them at church, at the school musical or at the local basketball game, they know they can talk with us and that we'll get the work done for them. We are willing to provide service that larger companies would never be able to cost-justify, such as dispatching an installer to make a home visit to help an elderly widow install her new Caller ID box, because we know it matters.

A second example of how a small, 26 employee company can have a much larger positive economic impact on its community is with the TeamQuest Corporation. When the Unisys Corporation closed its manufacturing facility in Clear Lake along with approximately 1,100 jobs, some of the local employees who liked Clear Lake's quality of life decided to spin off their own software development company. The TeamQuest Corporation has been able to expand to global markets and retain its headquarters in Clear Lake in part because of the telecommunications facilities we provide.

In contrast, we also know the harsh reality of a family business having to sell out to larger corporations. The Clear Lake Bakery, which was started by a German immigrant in the 1950s, grew to regional importance and employed over 300 people. But upon the passing of the founder, it was sold to a larger company which had numerous bakeries, was resold and ultimately was sold to a large regional baking company which decided to shut down the operation. Its empty storefront and warehouses in downtown Clear Lake are poignant reminders of what can happen.

We provide stable jobs to 26 professionals and their families. Most of these are long-term employees who share the vision of providing service to our community. We're proud of the fact that these hard-working employees have been able to make better lives for their children – like seeing them graduate from college. We relish the fact that we're a family-oriented business, that we have a chance to wish them happy birthday and attend their children's weddings and graduations and share life's important benchmarks with them.

In contrast, of all the companies which provide overlay competing services to our customers such as wireless companies, directory companies, business telephone system companies – none has an office in Clear Lake. To our knowledge not one employs a single Clear Lake resident. All of the revenues generated from their

customers here leave this small community and go to corporate headquarters elsewhere.

We feel it's important to give back to the community. We donate generously not only of our financial resources, but our time. My husband Tom and I are co-chairing a capital campaign to raise \$1.5 million for a library building expansion. It's a lot of money for a community our size, but we're driven to reach the goal because we believe in the library's important mission in a democracy such as ours. We know people who have encountered personal tragedies and have needed the services of the United Way and so we're a major contributor to this worthy organization, both financially and with volunteers.

Our schools need high speed Internet access to ensure that students will be well-equipped participants in the workforce and society so we provided free, high speed Internet access for the schools and a state of the art local area network; we are a major contributor to the local economic development corporation and to Opportunity Village, a residential facility for physically and mentally disabled; we've helped lead the way on improving our environment through recycling, Earth Day and lake water quality efforts. And our community provides public entertainment almost every weekend in the park, in part because of our regular sponsorship. We've been recognized as the corporate philanthropic organization of the year by a regional group, industry of the year by the local Chamber and other awards.

All of these factors are part of quality of life, a key reason to keep small companies such as ours in business instead of killing them with the death tax. That quality of life was important enough to me that 14 years ago I decided to leave my journalism career and make sure that a family member from my generation got involved in the business. I received hands-on experience working in all departments and commuted to Minneapolis for four years to obtain my master's degree in telecommunications. It's important to me to be part of an organization which has a positive ripple effect on our community – on our economy, our families and our daily lives. We're working hard to balance the demands of a fast-moving, high-tech society with old-fashioned service and basic family-centered values.

It's a commitment we've made in spite of the difficulties we encounter of trying to focus on what's best for our customers and our employees while also trying to ensure it won't all be taken away when the next estate tax bill comes due.

We first learned about this harsh possibility of losing everything while we were still mourning the passing of my grandmother Esther Woodford Ashland...

My name is Tom Lovell and I am the general manager and a vice president of the company.

It was shortly after December 4, 1984, when Jan's grandmother Esther Ashland died, that we discovered firsthand the potential crippling effect of the Federal Estate tax.

As was mentioned, our family was working with planners so we thought were prepared for the eventuality of the death tax. We soon saw the difficulty of the "fair market value" portion of the death tax as it applies to closely-held corporations. We filed a federal estate tax return showing a taxable estate of \$3,866,977, with a federal estate tax owing of \$1,404,772 and Iowa inheritance tax of \$266,565. The return was examined and the

IRS increased valuations by about \$1 million on our family farm and woodland and telephone company increasing the total taxable estate to \$4,988,717. This increased the federal estate tax burden to \$1,897,928 and Iowa Inheritance tax to \$390,366. Earl and Esther Ashland had done planning and purchased insurance, but it wasn't enough to cover the increased valuation.

In order to pay these death taxes and preserve the family farm and family owned telephone company, all of Esther's liquid assets and real estate except for her homestead were sold. The telephone company used all of its available liquid assets to redeem as much stock as possible. This left the telephone company with a minimal cash position with which to operate. The high estate values occurred because the farm and telephone company had to be valued at "fair market value" even though we had no intention of selling them. The century farm has a woodlands which had been a source of joy for many people for generations. But it includes a mile of undeveloped lakeshore and it was taxed at its "highest and best use or development potential" even though we never intended to develop it.

The valuation of a small, closely-held company is not easy to determine. We used experts who did an analysis of fair market value and yet the IRS did not accept this valuation. The majority of the investment in our company is in electronic switching and fiber and copper cables which have no other value except for use as a telephone company. We can't sell these assets off piecemeal. We are not a publicly traded company and therefore, it's difficult to get a per share value and find a comparable situation from a market value perspective.

Since the time of Esther Ashland's death, the family has spent an enormous amount of time, energy and money to prepare for the next imposition of estate tax when Jan's parents pass away. Fortunately, the state of Iowa has eliminated the inheritance tax on children and grandchildren, but the federal estate tax remains an imposing burden.

We have been able to implement some additional planning tools. After much research, we were able to place a conservation easement on the family woodland so it can never be developed and thus is not subject to a valuation that may force us to sell it or develop it. Because of this work, Lone Tree Woods will remain open for the public enjoyment as a natural area forever. In Iowa, public recreational lands are a rare commodity because our former prairies and wetlands are so highly productive for agriculture.

We have employed professional estate planners and attorneys from Minneapolis to help mitigate the financial impact that the next round of estate taxes will have on our company. The company has spent over \$3,000,000 in insurance premiums over the past eight years to fund a stock redemption program that will generate the cash to pay the projected federal tax burden. Not included in this figure is the money spent for professional assistance and the time spent on estate planning instead of running the company.

Unfortunately, we may not be able to accomplish our goal. The telephone company must keep operating and investing in its operations to remain viable in today's competitive environment. We have always prided ourselves on being able to provide the best technology at an affordable cost to our customers. But the costs of providing these services continues to escalate. For example, in 1955, we paid approximately \$225,000 for our Automatic Electric step switch. In 1995, it cost \$1.5 million to purchase our

second generation digital switch, an AT&T (now Lucent Technologies) digital switch. The useful life of a digital switch is now only seven years and replacement costs continue to escalate.

But we may have to choose between investing in our company to provide new services to our customers or setting aside funds to pay off the projected estate taxes. We can't do both. Our final choice may be to sell the company, which would be a loss to our employees and our community.

Some have said that with a little planning, no one pays any estate taxes. That is not true. Jan's grandparents, Earl and Esther Ashland planned and purchased insurance, her parents Marcia and Jim Connell have spent enormous financial and time resources and our families and Jan's sisters' families have as well. We have done an extraordinary amount of planning and we know there will be an enormous tax burden to pay. We have used and will continue to use revocable trusts, GRATS, charitable trusts and split dollar life insurance in hopes that we can keep our company intact. But the future is uncertain because of the company's ever-increasing "fair market" valuation that means so little to us but means everything to the IRS.

We are asking you to consider the severe impact the federal estate tax has on small family owned businesses such as ours. In the broader context, our situation is similar to that of family and locally owned businesses across the country. It's important to remember that small businesses are responsible for generating economic activity across the country. Small businesses create two-thirds of the new jobs in the United States, according to the National Federation of Independent Business. And 98% of the new businesses created in America are created by small business. Plus, 40 percent of the Gross Domestic Product is supplied by small business.

And our telephone company is just like hundreds of family owned telephone companies across the United States who are also on the front line managing their businesses day to day, trying their level best to provide advanced telecommunications for their communities. Countless hours and hundreds of thousands of dollars are spent annually to deal with death taxes when that time and money could be better spent operating our business.

We ask you to consider the impact on our employees and community if we are forced to sell our company to pay this exorbitant federal estate tax burden. We ask you to consider eliminating the death tax because it has consequences which were never intended - which is the forced sale of small, family owned businesses.

Thank you for your consideration.



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for you* **CL TEL**

Biographies for Representatives of Clear Lake Independent Telephone Company
March 2001

Thomas A. Lovell

Work Experience: Employed at the Clear Lake Independent Telephone Company, Clear Lake, Iowa since 1990. Currently serving as general manager and vice president. Partner in Stillman, Goranson, Stone and Lovell law firm in Clear Lake since 1981. Served as Assistant County Attorney for Goodhue County in Red Wing, Minnesota 1980-81.

Education: Graduated from Clear Lake Community Schools in 1972. Received BS in Economics from Drake University in Des Moines, Iowa, magna cum laude, in 1975. Member of Omicron Delta, national economics honor society. Received Juris Doctor degree from Northwestern School of Law Lewis and Clark College in Portland, Oregon in 1979.

Activities/Affiliations: Past president and current board member of Clear Lake Economic Development Corporation; past president of Legal Services Corporation of Iowa; past president of Clear Lake Lions Club; co-chair, Clear Lake Public Library Capital Campaign; past president of Board of Deacons and Board of Trustees of First Congregational Church; Cub Scout den leader; Little League coach; past president of Telnet Communications LLC of Des Moines; currently serve on Board of Managers of Midwest Wireless Holdings of Mankato, Minnesota; served on state and national trade organizations committees such as the Iowa Telecommunications Association and OPASTCO.

Personal Information: Married 23 years to Janet Lovell, one son, Christopher.

Janet C. Lovell

Work Experience: Employed at the Clear Lake Independent Telephone Company, Clear Lake, Iowa since 1986. Currently serving as assistant manager and vice president. From 1978-1986 worked as newspaper reporter and/or editor for newspapers in suburban Portland, Oregon; North St. Paul, Minn., Red Wing, Minnesota and Mason City, Iowa. Published freelance articles for national and regional magazines and numerous newspapers.

Education: Graduated from Clear Lake Community Schools in 1974. Received a BA from Lewis and Clark College in Portland, Oregon in 1978, Magna Cum Laude. Member of Phi Kappa Phi national honor society. Received M.S. in Telecommunications from St. Mary's University of Minnesota, in 1994 (Minneapolis campus).

Activities/Affiliations: Co-Chair, Clear Lake Public Library Capital Campaign; past president and trustee, Clear Lake Public Library Board of Trustees; past treasurer and director of Clear Lake Chamber of Commerce Board of Directors; trustee of North Iowa Area Community College Foundation board; served on Board of Deacons, Trustees and currently serve on Board of Christian Education at the First Congregational Church; chairperson of Clear Lake Earth Day; advisory board member of the Iowa Natural Heritage Foundation; past president of Sexual Assault Center; current member and former chair of the Telecommunications Advisory Committee to the Iowa Telecommunications and Technology Commission. Served on numerous committees of community organizations and state and national trade organizations.

Personal Information: Married for 23 years to Thomas Lovell, one son, Christopher.